Corporate Social Responsibility - Corporate Law Perspective

Introduction

1. CSR has proved to be boon or bane and whether the same can be forceful responsibility, the article analyses the situation in light of recent developments and after span of 5 years the dynamic law which the government thinks and re-thinks now and then.

Government of India made its first attempt to formally introduce concept of Corporate Social Responsibility (CSR) in 2009 with the issuance of Corporate Social Responsibility Voluntary Guidelines by the Ministry of Corporate Affairs (MCA, 2009). Later in 2011 again Ministry of Corporate Affairs tried to widen the scope of CSR by introducing National Voluntary Guidelines of Social, Environmental & Economic Responsibilities of Business. But till 2013 CSR regime remain unregulated, then in 2013 first time Ministry of Corporate Affairs made an attempt to codify and regularize the concept of CSR by introducing Section 135 of Companies Act which try to regularize spending as well as reporting of CSR activities by the companies.

Relevant provisions

2. Section 135 of Companies Act, 2013 says that:

(1) "Every company having net worth of rupees five hundred crore or more, or turnover of rupees one thousand crore or more or a net profit of rupees five crore or more during any financial year shall constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors, out of which at least one director shall be an independent director."

As per section 135 of the Companies Act, 2013 read with section 134 of the same Act, every company which falls under section 135(1) shall ensure that the company spends at least two per-cent of the average net profits of the company in every financial years and if fails to spend such amount, the Board of the company shall mention the reason of such failure in the report made under section 134(3)(o) of the Companies Act, 2013.

Section 134(3)(o) of the Companies Act, 2013 says that:-
(3) There shall be attached to statements laid before a company in general meeting, a report by its Board of Directors, which shall include— (o) the details about the policy developed and implemented by the company on corporate social responsibility initiatives taken during the year;

And if Board does not disclose the reason in its report then as per section 134(8) company shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees, or with both.

It means section 134 of the Companies Act, 2013 provide punishment only if company fails to comply with section 134(3)(o) regarding CSR disclosures [reason for not spending the amount as per section 135(5) of Companies Act, 2013] in Board's report. Except this there is no specific provision in Companies Act, 2013 that provide punishment for non-compliance of CSR responsibility given under section 135 of Companies Act, 2013. Therefore, in absence of any other specific provision for non-compliance of CSR responsibility Section 450 of Companies Act, 2013 will apply.

As there is no provision in Companies Act, 2013 which provide punishment for violation of Corporate Social Responsibility, company might be held liable for violation of CSR responsibility under section 450 of the Companies Act, 2013 which is a general provision and provide punishment for contravention of any provision of Companies Act, 2013 if punishment for that section is not specifically provided but it only impose penalty maximum upto ten thousand rupees. Hence except Section 450 of Companies Act, 2013 there is no any other provision which provide any penalty or punishment for violating CSR responsibility.

Residuary penalty provision is Section 450 of Companies Act, 2013 which reads as under –

"Punishment where no specific penalty or punishment is provided.—

If a company or any officer of a company or any other person contravenes any of the provisions of this Act or the rules made thereunder, or any condition, limitation or restriction subject to which any approval, sanction, consent, confirmation, recognition, direction or exemption in relation to any matter has been accorded, given or granted, and for which no penalty or punishment is provided elsewhere in this Act, the company and every officer of the company who is in default or such other person shall be punishable with fine which may extend to ten thousand rupees, and where the contravention is continuing one, with a further fine which may extend to one thousand rupees for every day after the first during which the contravention continues."

But if we analyse the general implication of Section 450 of the Companies Act, 2013, we find that rather imposing any penalty, it provides a better way or a legal route to any company to escape from the CSR responsibility.

For example- Suppose there is a company XYZ Pvt. Ltd. having average net profit of Rs. 10,000 crores in a year, now as per section 135 of Companies Act, 2013 XYZ Pvt. Ltd. has to spend Rs. 200 crores in every financial year as a CSR responsibility and as per section 450 of the Companies Act if he fails to spend Rs. 200 crores, maximum penalty of Rs. 10,000 will be impose on it. Therefore it is better for a company to pay Rs. 10,000 instead of Rs. 200 crores. Hence the ambiguity arises that whether company should pay only Rs. 10,000 as a penalty for violation of provision of Companies Act, 2013 or company should spend 2 per cent of the average annual net profit as well as penalty of Rs. 10,000.

**Report of the Legal Sub-Committee on CSR**

3. Report of the Legal Sub-Committee (constituted by Ministry of Corporate Affairs dated 04.04.2018) on Corporate Social Responsibility published on 26.04.2018 clarified that carry forward of unspent CSR amount would tantamount deferment of expenses and deferment as prescribed under Accounting
Standard(s) is possible only in respect of revenue expenditure or tax. Since CSR neither falls under revenue expenditure nor under tax expenditure, carry forward of CSR is improper as per Accounting Standard(s). Wherever it is reflected in books of account of the companies, company should either spent within a year or alternatively deposit it in Central Government Funds as provided in Schedule VII of the Companies Act, 2013.

**Violation of section 135 of Companies Act, 2013 attracts penal action?**

4. Under Companies Act, 2013 as per section 134(8) if a company covered under section 135(1) of the Companies Act, 2013 fails to mention the reason in Board’s report for not complying with the CSR responsibility, then only penal action will be taken against it.

Issues-

- Whether the reason which is mandatorily required to be mentioned in Board report for non-compliance of CSR responsibility should be any reason or there are some criteria to consider any reason as an acceptable reason.
- Section 135(5) of Companies Act, 2013 use words "Board shall ensure that company spends", therefore the word 'shall' shows the intention of the legislature to make CSR provision a mandatory provision. As construction of the provision or words used in the provision are the keys for opening the mind/intention of the Legislature, use of word "shall" create confusion in a way that section 135 of Companies Act, 2013 can be interpreted as mandatory provision and violation of it without any acceptable reason attracts penal actions.
- CSR- Corporate Social Responsibility the term in itself imposes a social responsibility on corporates. Therefore, it is a kind of duty or responsibility of companies, now question arise can violation of social duty/responsibility ever attracts penal consequences?

Report of the Legal Sub-Committee (constituted by Ministry of Corporate Affairs dated 04.04.2018) on Corporate Social Responsibility published on 26.04.2018 discussed on penal action as per section 134(8) of Companies Act, 2013 that as on 26.04.2018 there has not been any judicial ruling as regards valid, justifiable, demonstrable and more particularly acceptable "specific reasons". Use of words "shall ensure that company spends" in Section 135 of Companies Act, 2013 it becomes mandatory for the CSR eligible companies to spend the prescribed amount, failure of which shall attract penal action unless the regulatory authority accepts the reasons given in the report. Therefore, Committee Report considered section 135 to be a mandatory provision non-compliance of which attracts penal actions. Committee further recommends to adopt optimum compliance with minimum prosecutions approach by issuing show cause notice to companies for violation of CSR responsibility by adding a line that if that company deposits such amount to the Central Government Funds as per Schedule VII of the Act, Central Government shall not file prosecution against that company. In this way high level committee of CSR recommends to use penal action as a tool to achieve the goal of successful compliance of CSR responsibility by companies.

Recently, the Government has constituted the High Level Committee on Corporate Social Responsibility - 2018 (HLC-2018) for reviewing the existing framework and guide and formulate the roadmap for a coherent policy on CSR.

**5. Scope of HLC-2018**

(i) To review existing CSR framework as per Act, Rules and Circulars issued from time to time.
(ii) To recommend guidelines for enforcement of CSR provisions.
(iii) To suggest measures for adequate monitoring and evaluation of CSR by companies.
(iv) To examine and recommend audit (financial, performance, social) for CSR, as well as, analyze
outcomes of CSR activities/programmes/projects.

(v) Any other matter incidental or connected thereto.

The Committee shall submit its report within three months from the date of holding its first meeting. It will be interesting to see the outcome and consequential legal amendment.